

**Internal Revenue Service**

**199945046**  
Department of the Treasury

Index Numbers: 1031.03-00, 2032A.15-00

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:DOM:IT&A-PLR-122378-98

Date:

AUG 12 1999

Unique Identifying Number of Person to Contact:  
50-00388

Taxpayer:

Taxpayer's TIN:

Taxpayer's Address:

Decedent = :

Decedent's Spouse =

Revocable Trust M =

Revocable Trust F =

Property A =

Tract 1 =

Tract 2 =

Year 1 =

Year 2 =

Year 3 =

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Dear

This responds to a request for a letter ruling dated October 12, 1998, which was submitted by you on behalf of Taxpayer. Your request relates to the federal income tax consequences under § 1031 of the Internal Revenue Code and the federal estate tax consequences under § 2032A of the Code of a proposed exchange of interests in a single parcel of real property (Property A). The proposed exchange is between Taxpayer and Revocable Trust F. Each party currently owns an undivided one-half interest in Property A as tenants in common. The proposed exchange will result in Taxpayer owning a 100 percent fee simple interest in one-half of the property (Tract 1) and Revocable Trust F owning a 100 percent fee simple interest in the other one-half of the property (Tract 2).

In Year 1, Decedent and Decedent's Spouse each owned a one-half undivided interest in Property A, which was used for ranching operations. In Year 1, Decedent's Spouse conveyed his undivided one-half interest in Property A to Revocable Trust F. Decedent's Spouse is the grantor, trustee, and beneficiary of Revocable Trust F.

Also in Year 1, Decedent's one-half undivided interest in Property A was conveyed to Decedent's Revocable Trust M, which became irrevocable upon her death in Year 2. Decedent's one-half undivided interest in Property A was included in Decedent's gross estate and, on the federal estate tax return filed for the estate, the executor elected special use valuation under § 2032A for valuing the includible interest. Taxpayer received his interest in Property A from Decedent's estate in Year 3. Taxpayer is the son of Decedent and Decedent's Spouse.

Property A has been used exclusively for ranching. There are a few minor improvements on Property A, and they are directly related to ranching. There are no mortgages or liens, except for that of § 6324B, on Property A.

Prior to the time Taxpayer received his interest in Property A, he was an employee of the trustee of Revocable Trust F and helped to operate the trustee's herd on Property A. After Taxpayer received his interest in Property A, and at the same time received additional cattle, he operated his own herd on Property A. The trustee of Revocable Trust F continued to operate his herd on Property A. The herds are separately identifiable, each having a different brand. Taxpayer contributes the substantial majority of the ranching labor in return for his operation of a herd that is slightly larger than the trustee's herd on Property A. Taxpayer and the trustee do not purport to operate any aspect of their ranching businesses as a partnership. Taxpayer and the trustee account for their ranching operations separately and file a separate Schedule F (Profit or Loss From Farming) with their individual Form 1040 income tax returns.

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Property A will be divided into two areas, Tract 1 and Tract 2, which are as nearly equal in size and value as can possibly be arranged. It has been represented that both Taxpayer and the trustee of Revocable Trust F believe that the exchange as proposed would be equal in value (and takes into account the few minor improvements consisting of a 24' by 36' metal shed and a livestock corral).

Taxpayer and Revocable Trust F propose that they complete a simultaneous exchange of interests in Tract 1 and Tract 2 so that Taxpayer will own a 100 percent of Tract 1 and Revocable Trust F will own a 100 percent of Tract 2. The transfer of ownership will be accomplished by the exchange of quitclaim deeds in favor of each other to the property they are transferring. No formal process other than the exchange and recording of quitclaim deeds is required. No subdivision of Property A is necessary. No cash or other property will be involved in the exchange.

The purposes for the exchange are to unify ownership interests and ease future estate planning, as well as ease use and accounting for ranch properties. Taxpayer represented that the property he will own after the proposed exchange would continue to be used for ranching.

Section 2032A(a)(1) provides, in part, that, if the decedent was a citizen or resident of the United States at time of death and the executor elects the application of § 2032A and files the agreement described in § 2032A(d)(2), the value of qualified real property included in a decedent's estate shall be its value for the use under which it qualifies as qualified real property rather than its fair market value.

Section 2032A(b)(1) provides, in part, that "qualified real property" means real property acquired from or passed from the decedent to a qualified heir of the decedent and which, on the date of the decedent's death, was being used for a qualified use by the decedent or a member of the decedent's family.

Section 2032A(b)(2)(A) provides, in part, that the term "qualified use" means the devotion of the property to use as a farm. Section 2032A(e)(4) provides that the term "farm" includes, among other things, ranches.

Section 2032A(c)(1) provides that if, within 10 years after the decedent's death and before the death of the qualified heir, the qualified heir disposes of any interest in qualified real property (other than by a disposition to member of his family), or the qualified heir ceases to use the qualified real property for the qualified use, then there is imposed an additional estate tax.

Section 2032A(e)(2) provides that the term "member of the family" means, with respect to any individual, only (A) an ancestor of such individual, (B) the spouse of such individual, (C) a lineal descendant of such individual, of such individual's spouse, or of a parent of such individual, or (D) the spouse of any lineal descendant described in

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subparagraph (C). For these purposes, a legally adopted child of an individual shall be treated as the child of such individual by blood.

Section 2032A(c)(5) provides, in part, that the qualified heir shall be personally liable for the additional tax imposed with respect to his interest.

Section 2032A(i)(1)(A) provides that, if an interest in qualified real property is exchanged solely for an interest in qualified exchange property in a transaction which qualifies under § 1031, no tax shall be imposed by § 2032A(c) by reason of such exchange.

Section 2032A(i)(3) provides that the term "qualified exchange property" means real property which is to be used for the qualified use set forth in § 2032A(b)(2)(A) or (B) under which the real property exchanged therefor originally qualified under § 2032A(a).

Thus, if an interest in qualified real property will be exchanged solely for an interest in qualified exchange property in a transaction that qualifies under § 1031, no tax shall be imposed by § 2032A(c) by reason of such exchange. Moreover, because Revocable Trust F is a revocable trust and Decedent's Spouse is the grantor, trustee, and beneficiary of Revocable Trust F, Decedent's Spouse is treated as the owner of the entire trust under § 676. In this regard, Taxpayer's transfer of his interest in Property A to Revocable Trust F is a transfer to his father, who is a member of Taxpayer's family within the meaning of § 2032A(e)(2). Thus, regardless of whether the property exchange qualifies under § 1031(a)(1), there would be no imposition of the additional estate tax described in § 2032A(c)(1) because that provision permits a qualified heir to dispose of qualified real property to a member of the qualified heir's family.

Section 1031(a)(1) provides the general rule that no gain or loss shall be recognized on the exchange of property held for productive use in a trade or business or for investment if such property is exchanged solely for property of like kind which is to be held either for productive use in a trade or business or for investment. Section 1031(a)(2) provides certain exceptions. See also § 1.1031(a)-1(a) of the Income Tax Regulations.

Section 1.1031(a)-1(b) provides that the words "like kind" have reference to the nature or character of the property and not to its grade or quality. One kind or class of property may not, under § 1031, be exchanged for property of a different kind or class. The fact that any real estate involved is improved or unimproved is not material, for that fact relates only to the grade or quality of the property and not to its kind or class. Unproductive real estate held by one other than a dealer for future use or future realization of the increment in value is held for investment and not primarily for sale.

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In Rev. Rul. 73-476, 1973-2 C.B. 300, three individual taxpayers each owned an undivided interest as a tenant in common in three separate parcels of real estate for investment purposes. Each of the taxpayers exchanged his undivided interest in the three separate parcels for a 100 percent ownership of one parcel. Each taxpayer continued to hold the single parcel of land as an investment. The revenue ruling holds that none of the taxpayers would recognize any gain or loss pursuant to § 1031(a).

In Rev. Rul. 79-44, 1979-1 C.B. 265, two unrelated individuals owned undivided one-half interests in two separate parcels of land as tenants in common. Both parcels were used in the taxpayers' business of farming. One parcel was subject to a mortgage. The parties rearranged their interests so that each owned 100 percent of a separate parcel. One party executed a promissory note to the other to compensate him for taking the property subject to the mortgage. The parties continued to use the parcels in their respective businesses of farming. The revenue ruling holds that the property interests exchanged are like kind property and the provisions of § 1031 apply to determine to what extent, if any, the gain is to be recognized.

\* \* \* \* \*

Based on the information submitted and the authorities cited above, we rule as follows:

- (1) Taxpayer's proposed exchange of his undivided one-half interest in Tract 2 for Revocable Trust F's undivided one-half interest in Tract 1 qualifies as a like kind exchange under § 1031.
- (2) No tax shall be imposed by § 2032A(c).

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the material submitted in support of the request for rulings, and it is subject to verification on examination.

This letter ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

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A copy of this letter ruling must be attached to any tax return to which it is relevant.

Sincerely,

Acting Assistant Chief Counsel  
(Income Tax and Accounting)

By Kelly Alton  
Kelly Alton  
Senior Technician Reviewer,  
Branch 5

Enclosures (2):  
Copy of this letter  
Copy for section 6110 purposes